

BILL # SB 1025

TITLE: income tax exemption; military pensions

SPONSOR: Harper

STATUS: As Amended By Senate FIN

PREPARED BY: Hans Olofsson

FISCAL ANALYSIS

Description

Under current law, a taxpayer is allowed a state income tax exemption of up to \$2,500 for U.S. military retirement and retainer pay. SB 1025 would remove the cap and allow the full retirement amount to be exempted from Arizona income tax. In addition, the bill would also exempt military survivor benefits from state income tax. The bill, as amended, would become effective in tax year 2008.

Estimated Impact

Beginning in FY 2009, the bill is estimated to reduce individual income tax collections by \$(26.6) million.

Analysis

According to federal fiscal year (FFY) 2005 data released by the United States Department of Defense (DOD), Arizona has 49,200 military retirees paid an average of \$21,200 annually by DOD. In addition, the state has 7,300 recipients of military survivor pay receiving an average of \$9,100 annually.

Assuming that each of these military retirees already claim an exemption of \$2,500 under current law and will claim their full military pension under SB 1025, it is estimated that the individual income tax loss will be an estimated \$(24.8) million $[=49,200 \times (\$21,200 - \$2,500) \times 0.027]$ beginning in FY 2009. This estimate assumes an average marginal tax rate of 2.7% for military retirees.

According to the Department of Revenue (DOR), survivor benefits are not exempt from state income tax under current law. For this reason, this provision of the bill is estimated to reduce individual income tax collections by about \$(1.8) million $[=7,300 \times \$9,100 \times 0.027]$ beginning in FY 2009.

The total estimated General Fund revenue loss is thus estimated to be \$(26.6) million beginning in FY 2009.

Local Government Impact

Each year, incorporated cities and towns receive 15% of income tax collections from 2 years prior. This bill would reduce local government distributions by \$(4.0) million beginning in FY 2011.